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DUN'S BUSINESS MONTH

Penn Central Rides High

October 1981 $2.25

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Those Lucrative Employment Contracts

Protectionism Rises in Europe

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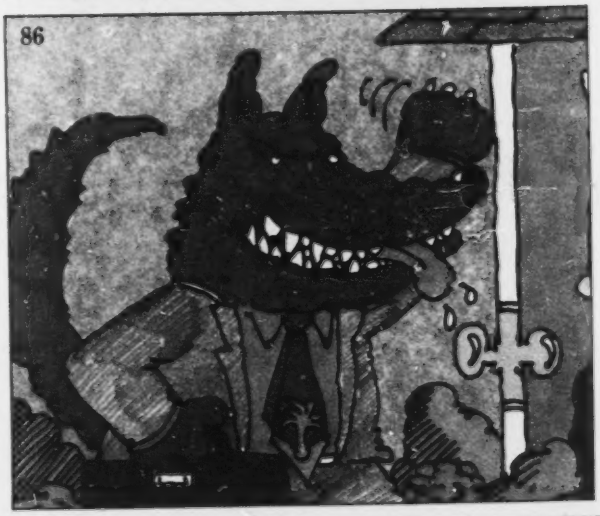

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rate in the 1980s, compared with the 7¼% yearly rise before the 1973 oil embargo.

The fall-off in new construction is crucial to the new utility economics. The industry discovered that inflation wiped out past economies of scale gained from investment in new plant because 60% of new capital spending was raised externally. Each new bond sale pushed up the costs of debt while each stock offering sold below book value diluted the equity. Now, slower growth in capital spending should mean fewer financings, which in turn should help bring rates down.

Liu believes investors can play the utility group turnaround in several ways: for high-quality growth, high yield, superior dividend growth or short-term capital gains. Among the high-quality utilities, he prefers Texas Utilities Co., Northern States Power Co., Wisconsin Power & Light and Southwestern Public Service. These companies, he says, have highly visible earnings growth rates of two-to-three percentage points above the average utility. Despite their recent price gains, their price/earnings ratios are still no higher than the rest of the group. Thus they have the potential for an improvement in their multiples if inflation declines.

Among relatively high-yield issues, he thinks the safest plays are Baltimore Gas & Electric, New England Electric Systems and Duke Power Co. Liu notes that Duke will increase its cash flow because it is selling off part of its investment in new facilities to other utilities.

Among companies that will see the best dividend growth, he likes Consolidated Edison, Southern California Edison and TECO Energy (formerly Tampa Electric). These companies have been very conservative in their dividend policies and will probably see the need to increase their payout ratios to nearer the industry average.

Con Edison, for example, is currently yielding about 10%, but its dividend of $2.92 is roughly half of its estimated 1981 earnings of $5.75 a share (the typical utility pays 80% of current earnings in dividends). Con Edison recently won a $450 million rate increase, which should swell earnings sufficiently to permit a 10% dividend hike in January, Liu says. He expects it to produce a 20% overall return.

Of high-yielding, slightly riskier utilities that should be good plays on a downturn in interest rates for a three-to-nine month holding period, Liu suggests Commonwealth Edison, Virginia Electric Power, Carolina Power & Light, Pacific Gas & Electric, Illinois Power, Delmarva Power & Light and Middle South Utilities. Liu chooses these issues because, he believes, "They will give near-term a bigger bang for the buck, have relatively good yields and are not in danger of shaving the dividend." —A.H.

INVESTMENT UPDATE

Here's the current status of a number of investments, and a look at how they have fared over the past month and the past year.

Investment	(8/31/81) Recent Price	Value of $10,000 if invested: Month Earlier	Year Earlier
Common Stock (Index fund, capital gains and dividends reinvested)	$16.33/share	$ 9,456	$ 10,516
per cent change		−5.4%	+5.2%
Bonds (30-yr., 11¾% Treasury Bond)			
MARKET VALUE	$80.438	$ 9,498.16	$ 7,814.22
ACCUMULATED INCOME		$ 116.00	$ 1,141.00
TOTAL		$ 9,614.16	$8,955.22
per cent change		−3.86%	−10.45%
Money Market Fund	17.18%	$10,122.83	$11,577.77
per cent change		+1.22%	+15.77%
Gold (Krugerrands)	$448.25/oz.	$10,511.46	$ 6,750.85
per cent change		+5.11%	−32.49%
House (new single family)	$98,100	$ 95,200	$ 88,600
per cent change		+3.05%	+10.72%

Sources: Vanguard Group Inc.; Salomon Brothers; Donoghue's Money Fund Report of Holliston, Mass. 01746; Desk-Perera Fifth Avenue, Inc.; Federal Home Loan Bank Board.

Tax Break on Utility Dividends

Among the many advantages of the new tax bill, one has gone almost unnoticed. Beginning January 1, shareholders who participate in the dividend reinvestment plans of public utilities will be able to defer paying taxes on their dividends.

Specifically, a shareholder who elects to receive stock instead of cash dividends can exclude those dividends from his taxable income up to a limit of $750 a year, or $1,500 in a joint return. If the shares are held for at least a year, they are taxed as long-term capital gains—now reduced to a maximum rate of 20%—when sold. (Shares held for less than a year are taxed as ordinary income, thus negating the tax advantage.)

The way the law is written, nearly all electric, natural gas and water companies qualify for tax-deferred plans, but most telephone companies do not. However, several electric companies with large non-utility holdings may be ineligible. Only original-issue dividend reinvestment plans qualify for the special tax treatment; that is, the shares must be newly issued by the company, not purchased on the open market.

—M.S.L.